



# Economic Update

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Volume 4, Number 9

14 December 2005

## ROBUST GROWTH CONTINUES

### Overview

The economy's rapid 4.3-percent growth in the 3<sup>rd</sup> quarter reinforced the expansion's robust pace, as well as forecasters' expectations of continued healthy growth in the future. Labor productivity also grew at a rapid pace, reflecting strong growth in output with increased hours worked. Payroll employment showed a large gain in November. In addition, indications are that business activity in the manufacturing and services sectors of the economy continues to expand at a solid pace.

### Highlights

- The inflation-adjusted (real) gross domestic product [GDP] grew at a rapid 4.3 percent in the 3<sup>rd</sup> quarter. Forecasters see healthy, 3.2 percent growth in the 4<sup>th</sup> quarter, and strong growth throughout 2006 (Fig. 1).
- Employment posted strong growth in November, with 215,000 new jobs added to the Nation's payrolls (Fig. 2, next page). Unemployment was 5.0 percent in November.
- Productivity (output per unit of labor) in the non-farm business sector rose at a rapid 4.7 percent annual pace in the 3<sup>rd</sup> quarter. Productivity gains are key to growth in wages and living standards.
- The Federal Reserve, as expected, raised its target overnight interest rate another 0.25 percent – and also indicated that further increases are likely.

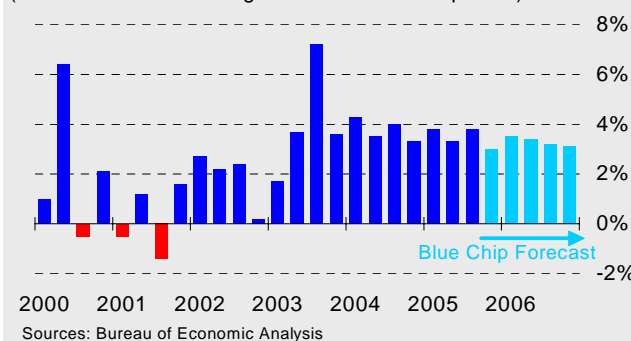
### Third-Quarter Growth Remains Strong

The 4.3-percent growth rate in the 3<sup>rd</sup> quarter was led by consumer spending, business investment, Federal Government spending, and residential investment. Inventory investment fell for the second consecutive quarter as businesses met demand by drawing down inventories. This bodes well for future growth as businesses produce more to restock their shelves.

### Economic Growth Since 2000

(Real annualized GDP growth rate in each quarter)

Fig. 1



### Blue Chip Economic Outlook, November 2005

	2005				2006			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	Actual				Projection			
Real GDP Growth	3.8	3.3	4.3	3.2	3.5	3.4	3.1	3.1
Unemployment Rate	5.3	5.1	5.0	5.0	5.0	4.9	4.9	4.9
CPI Inflation	2.5	4.0	5.3	3.9	2.2	2.4	2.3	2.3
3-month Treas. Bill	2.5	2.9	3.4	4.0	4.4	4.5	4.6	4.6
10-year Treas. Note	4.3	4.2	4.2	4.6	4.8	4.9	5.0	5.0

Forecasters continue to see healthy growth in – and low inflation. The *Blue Chip* consensus forecast is for annualized growth in real GDP to slow to a still-healthy 3.2 percent in the 4<sup>th</sup> quarter. Growth is then expected to remain above 3.0 percent throughout next year.

GDP is a broad measure of the Nation's output of goods and services. Growth in real GDP has been at or above 3.3 percent for 10 consecutive quarters. Ten uninterrupted quarters of real GDP growth above 3.0 percent is the longest such stretch since the 13 quarters that ended in the 1<sup>st</sup> quarter of 1986.

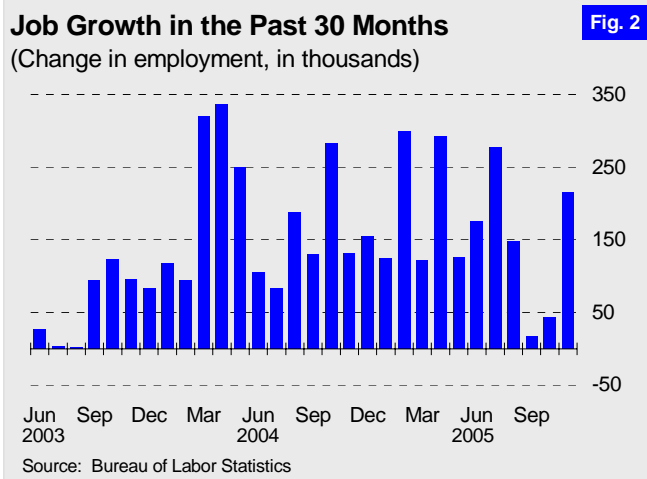
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## Employment Increases

Payroll employment rose by an appreciable 215,000 new jobs in November as labor markets rebounded from two months of only modest gains. The Bureau of Labor Statistics has noted that weak job growth in September was “largely due to the job loss in areas devastated by Hurricane Katrina.”



There have been 30 consecutive months of payroll job gains, adding close to 4.5 million new jobs to the Nation's payrolls. Over 1.8 million new payroll jobs have been added so far this year. The unemployment rate remained at 5.0 percent in November, well below the average in each of the past three decades

## Expansion Continues in Manufacturing and Services

The Institute for Supply Management [ISM] index of manufacturing activity fell slightly to 58.1 in November from 59.1 in October, but continues to show a vibrant pace of expansion in manufacturing. An index value above 50 indicates expansion in the manufacturing sector; a value close to 60 indicates a vibrant pace of expansion. The ISM manufacturing index has been above 50 for 30 consecutive months.

The ISM index of non-manufacturing (services) activity also eased somewhat in November, to 58.5 from 60.0 in October, but continues to indicate robust expansion in the services sector of the economy. The non-manufacturing index has indicated expansion in the services sector of the economy for 32 consecutive months.

## Productivity Growth Surges in the 3<sup>rd</sup> Quarter

Non-farm labor productivity grew at a rapid annualized rate of 4.7 percent in the 3<sup>rd</sup> quarter, more than double the 2.1-percent growth registered in the 2<sup>nd</sup> quarter. Historically high productivity growth in the last five years has been a central driver of overall economic growth. Productivity gains have averaged 3.28 percent annually between 2000 and 2004, compared with an average of 2.08 percent from 1995 to 1999 and 2.28 percent from 1948 to 2004.

## Household Net Worth Sets Record

The total net worth of households and nonprofit organizations rose 2.7 percent in the 3<sup>rd</sup> quarter to a record high of \$51.1 trillion, surpassing the previous record established in the 2<sup>nd</sup> quarter. Household net worth has risen for 12 consecutive quarters.

## Consumer Confidence Continues to Rebound

Measures of consumer confidence have rebounded from their post-hurricane declines, aided by declining gasoline prices and an improving job market. The preliminary December value of the University of Michigan Consumer Sentiment Index rose to 88.7, up from 81.6 in November and a post-hurricane low of 74.2 in October. A consumer sentiment measure compiled by the Conference Board also rebounded last month from its post-hurricane low. Consumer confidence is monitored given the importance of consumption in the economy; consumer spending accounts for around 70 percent of the Nation's total output.

## Fed Raises Rates; Further Increases Likely

With the 0.25-percent increase on Tuesday, the Federal Reserve has raised its target overnight interest rate from 1.00 percent to the current 4.25 percent in a sequence of quarter-point increases that began at the end of June 2004. More significant, however, was the Fed's policy statement, which removed the mention of “policy accommodation” [keeping rates low to accommodate increased economic growth] that had been included since May 2004. The Fed now states that “some further measured policy firming is likely to be needed.” This indicates that further increases in short-term interest rates are likely. The Fed also noted in its recent policy statement that despite elevated energy prices and economic disruptions related to the Gulf Coast hurricanes, the economic expansion appears solid. The next meeting of the Fed's monetary policy committee is scheduled for 31 January 2006.

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